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TAGS: EINV ECON EIND PGOV FR
SUBJECT: ECONOMIC PATRIOTISM, ECONOMIC INTELLIGENCE, AND PROTECTING FRANCE'S CORPORATE "JEWELS"

REF: 04 PARIS 0626

Classified By: Kenneth Merten, ECON, for reasons 1.4 (b) and (d).

Summary

¶1. (C) As reported reftel, the GOF continues to enact elements of Parliamentarian Bernard Carayon's "economic intelligence" program, as prescribed in his 2003 report. An important next step will be debate and ultimately passage of legislation (inspired by the U.S. Exon-Florio laws) which would define which industrial sectors merit protection from foreign control for "national security" reasons. The legislation is also set to establish a mechanism for vetting attempted takeovers. The rumored July takeover of Danone by PepsiCo and Prime Minister de Villepin's public defense of France's national "jewel" has been the business story of the summer in France. However, de Villepin's call for protection of Danone can be explained as much by political opportunism as by his belief that Danone is a "strategic" company that needed protection. De Villepin, Carayon, and others in the GOF continue to see France as having fallen behind competitors such as the U.S. and they are determined to give the GOF the tools necessary to support strategic sectors. The French private sector is far from unified in its support for de Villepin's pronouncements on Danone; some appreciate the government attention, while others are wary of interference in the market. As discussion of the foreign takeover legislation proceeds his autumn, it is in the USG's interest to urge the French to learn from our experience - both good and bad - with Exon-Florio (and CFIUS) and to stress the primary importance of shareholder rights and the role of the market. End Summary.

The Danone Case: Perfect for Grandstanding...

¶2. (U) In late-July 2005, when PepsiCo was rumored to have been considering a hostile takeover of French food group Danone, Prime Minister Dominique de Villepin issued a veiled warning to any potential foreign bidders, declaring that Danone was one of France's industrial "jewels" and saying that the GOF will strive "to defend the interests of France."

¶3. (C) The current government's emphasis on employment creation combined with the public's fears of outsourcing and job losses created the perfect backdrop for what French economist Elie Cohen has described as Danone's carefully orchestrated campaign against a Pepsi takeover "threat." While Danone could hardly be construed as a strategic company, President Chirac and PM de Villepin may have seen an excellent - and cost free - opportunity to score political points by publicly "defending" a French company with a call to "economic patriotism." Last year, then-Finance Minister Sarkozy initiated a similar public response by persuading Novartis, the Swiss pharmaceutical group, not to bid for Aventis against Sanofi, a French rival.

¶4. (SBU) While the media focused on the symbolism of a situation pitting a French water and dairy group against a U.S. soft-drink giant, Chirac and Villepin pointed to the need to reinforce the capital of large French corporations by amending French commercial law, implementing the EU Takeover Directive, and introducing American-style institutional pension funds in France. These measures were first outlined in Carayon's 2003 report (reftel) on "Economic Intelligence, Competitiveness and Social Cohesion," commissioned by then-Prime Minister Jean-Pierre Raffarin.

...But Linked to Increased Foreign Ownership of French Firms

¶5. (C) Referring to Danone-Pepsi in a typically equivocal statement, President Chirac said that while "it was out of the question to oppose any takeover of a French company per se," he said he remained concerned about the lack of a solid core of French shareholders among major French corporations such as Danone. The lack of French capital in French companies, he said, had a potentially negative impact on the French industrial base and thereby on employment. Chirac's statement draws attention to a problem long emphasized by French economists: the fragmentation of shareholding as France moved away from the stable cross-holding networks of its national champions in the late 1980s and 1990s. Some

French economists have argued that the opportunities created by French privatizations have mostly benefited foreign investors because of France's lack of institutional pension funds. By 2003, the CAC40 (the top forty companies quoted on the Paris stock exchange) was more than 50 percent foreign-owned, with around a quarter of the shares in U.S. and British hands. This trend has increased in recent months, according the latest study by French financial consultancy TLB. This study shows that foreign investment funds owned 61.4 percent of the shares of companies in the CAC40 index last June, an increase from 55 percent in March ¶2005.

¶6. (SBU) In fact, many icons of French capitalism are already owned by foreigners. With no fanfare, U.S. investment fund Starwood Capital recently acquired French luxury group Taittinger, which produces champagne and owns the historic Crillon Hotel, which had been the last five-star hotel in Paris still in French hands. Danone, allegedly targeted by Pepsi, is 42 percent owned by foreign investors, including the 24 percent stake held by U.S pension funds. Construction firm Lafarge, chaired by Jean-Louis Beffa, is 50.44 percent owned by non-French investors. All in all, France's National Economic Statistics Institute INSEE concludes that some 17,000 companies out of a total of 2.5 million companies (mostly small or very small companies) are owned, 50 percent or more, by foreign investors.

"Economic Patriotism" Not Universally Supported
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¶7. (C) It would be wrong to assume that Chirac and de Villepin's statements about Danone and "economic patriotism" - a phrase first coined by Carayon in 2003 - were universally supported. Many in the private sector (and some in government) lamented the government's public interference in what should have been a shareholder decision. Finance Minister Breton told us that he did not support the positions taken by "some politicians." He stated publicly that France benefits from foreign investment and that the country has a legal framework in place to handle takeovers. The government's job, he said, should be to ensure that the laws were obeyed.

¶8. (SBU) In the private sector, several CEO's have publicly warned the GOF against a possible drift towards "economic nationalism." Some observers liken France's "economic intelligence" drive to traditional state interventionism or Gaullist-style industrial policy. The policy has already driven a wedge between the "patriotic" CAC40 CEOs (Arnaud Lagardere of defense giant Lagardere, Jean-Francois Dehecq of Sanofi-Aventis, and Jean-Louis Beffa of glass firm Saint Gobain) and the strictly pro-market proponents (Hubert de Castries of Insurance firm AXA, Jean-Rene Fourtou of Vivendi Universal, and Patrick Ricard of drinks giant Pernod Ricard) who are wary.

¶9. (SBU) Some in the private sector have also noted that French concern about foreign takeovers of national champions is hypocritical given several recent high-profile foreign acquisitions by French companies. For instance, recently, France Telecom successfully fought off two powerful equity consortiums in order to buy 80% of Amena, the Spanish mobile phone group, for 6.4 billion euros. So far this year, French acquirers have bought foreign businesses worth almost $34 billion, higher than the $28 billion for all of last year, marking the highest level of activity since the height of the 2000 bull market, according to economic data and analysis company Dealogic.

Pending Economic Intelligence Legislation

¶10. (SBU) France's "economic intelligence" policy also plans to tighten foreign investment controls. French legislation on foreign investment has been revised three times since the Carayon report was first published in 2003 and we expect it to be further strengthened by government decree in September. Currently, Article 151-3 of the French Monetary and Financial Code provides that the Ministry of Economy and Finance must approve all foreign investment that a) could impair France's public order, public security, or national defense interests, and b) is related to the research, production or selling of arms, ammunitions, powders and explosive substances. Special conditions can be attached to the Ministry's authorization to ensure that the planned investment does not undermine France's national interest. A GOF refusal can be appealed before a French administrative judge. The penalty for an investor who contravenes these rules can amount to up to double the illegal investment.

¶11. (SBU) A Government decree is being drafted which will seek to further define the strategic sectors where foreign acquisitions require government authorization. These restrictions could cover companies involved in defense, biotechnologies related to combating terrorism or pathogen agents, the security of information systems, cryptography, as well as activities concerning dual-use technologies. The

decree could also redefine the threshold for "control" of a company, currently set at 33.33 percent. A condition might be added against a foreign investor holding less than a third of a French company but likely to "exert a decisive influence." Article 151-3 of the French Monetary and Financial Code has already prevented two U.S. companies from acquiring French producers of aeronautics components and night vision equipment.

¶12. (SBU) As part of his on-going push to protect strategic industries in France from foreign control, National Assembly member Bernard Carayon is organizing a colloquium on 10 October entitled, "Foreign Investment and National Security." The colloquium, to which Embassy and U.S. Treasury Department officials have been invited to speak, will address the possibility of creating a French equivalent to the Committee on Foreign Investment in the United States (CFIUS) and a French version of the Exon-Florio provisions. Embassy encourages USG participation in this timely colloquium and would welcome talking points on these issues.

Other Related Initiatives

¶13. (SBU) Last March, France's Senior Economic Intelligence official Alain Juillet announced a new investment fund to support unquoted strategic start-ups in the defense sector. The two-tier system involves public and private players. A select committee made up of representatives of France's strategic ministries (Economy, Foreign Affairs, Research, Defense, Interior) will choose the start-ups that will benefit from the expertise of three management funds (called Occam, Emertec Gestion and ACE Management). The Government select committee ensures that investment decisions will be made on the basis of France's national interest. The funds will focus on projects in information technology, security, aeronautics, defense and nanotechnology.

¶14. (SBU) As "economic intelligence" developed into a more comprehensive public policy last year (reftel), the French government began creating economic intelligence units in the several French ministries, beginning with the Economy, Finance and Industry Ministry, which set up a "General Delegation for Economic Intelligence" in October 2004. Headed by Francois Asselineau, the office has already played a leading role in drafting upcoming investment control legislation. Last December, then-Foreign Affairs Minister Michel Barnier appointed former Minister-Counselor for Economic and Commercial Affairs at the French Embassy in Washington, Jean-Baptiste Main de Boissiere to be the Foreign Ministry's new "Delegate General for Economic Intelligence." Boissiere's job will be to develop contacts and exchange information at the EU level and to train French diplomats in "economic intelligence".

¶15. (SBU) In addition to beefing up its central bureaucracy, Prime Minister de Villepin has asked all French prefects to be on the lookout for small and medium-sized strategic companies within their jurisdiction. The Interior Ministry will coordinate the actions by prefects (local national government representatives) with local authorities and private sector actors as part of the government's "territorial intelligence" effort in nine French pilot regions. France's private sector will also launch a structure of its own this fall, with the French Federation of Economic intelligence set up by former counter-intelligence Chief Admiral Pierre Lacoste.

Comment

¶16. (C) The current government believes that its "economic patriotism" and "economic intelligence" approaches are fully justified by the need to allay the French people's fears of high unemployment and a loss of national identity. Ironically, the GOF is as much on the offensive against its own antiquated laws, which prevent the development of a business and shareholding culture in France, as it is against what it considers to be outside threats to its national economic interests. Carayon's October colloquium on the upcoming takeover law revisions is "inspired" by the U.S. experience with controlling foreign investment through the Exon-Florio Act. Carayon's "economic intelligence" proposals seek to level the playing field with France's trading partners. Much of what the report suggests can help France reform outdated legislation and practices. However the whole nature of the "economic intelligence" exercise and the Carayon Report's imperfect understanding of the tools at other countries' disposal, lends itself to demagoguery and distortion. (His report was cited in articles in early 2005 in a regional newspaper implying that the Embassy's APP's were part of an organized U.S. economic intelligence effort to spy on key French firms.) Our challenge in France will be to ensure that there is an appropriate understanding and characterization of U.S. practices and policies. End Comment.

Hofmann